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No. 95-16

In the Supreme Court of the United States

OCTOBER TERM, 1995

MARTIN L. MANDEL, PETITIONER

v.

FEDERAL DEPOSIT INSURANCE CORPORATION, ETC.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether the court of appeals correctly concluded that petitioner had waived his contention that the district court applied an incorrect burden of proof.

2. Whether, in a civil suit brought by the FDIC to recover damages caused by petitioner in his capacity as director of a failed savings and loan institution, petitioner was entitled to raise state-law affirmative defenses of failure to mitigate damages and contributory negligence by the FDIC.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 7a-14a) is reported at 38 F.3d 1119. The findings of fact and conclusions of law of the district court (Pet. App. 15a-68a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on October 18, 1994. A petition for rehearing was denied on February 1, 1995. Pet. App. 3a-6a. On April 17, 1995, Justice Breyer entered an order extending the time within which to file a petition for a writ of

certiorari to and including June 30, 1995, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This case arises out of petitioner's actions as a member of the board of directors of State Savings and Loan Association of Utah (State Savings), a federally insured savings and loan institution, between October 28, 1983, and June 6, 1984. During that time, petitioner was senior vice president and counsel of Investment Mortgage International (IMI), which provided financing for real estate development projects. He was also involved in the management of Empire State West (Empire), which developed real estate. Pet. App. 18a-19a. At the relevant times, State Savings, IMI, and Empire were all owned and controlled by J. William Oldenburg. *Id.* at 18a.

During the fall of 1983, IMI undertook to obtain $50,000,000 in financing for the initial phase of the development, by Empire, of property known as Park Glen. At that time, IMI's financial condition was rapidly deteriorating due to extravagant expenditures, and IMI urgently needed $10,000,000 to continue operations. Pet. App. 44a-45a, 49a. The chief financial officer of IMI attempted to borrow $10,000,000 from State Savings, but he was rebuffed by the bank's president, who told him that the loan would be illegal because of Oldenburg's relationship to both entities. *Id.* at 45a. State Savings's officers and directors agreed, however, to purchase something from Oldenburg or his entities for the purpose of channeling the needed funds to IMI, and petitioner, Oldenburg, and other managers of IMI concluded that

selling the Park Glen property would provide the necessary infusion of cash. *Id.* at 46a.

Accordingly, on January 31, 1984, State Savings entered into a contract with Empire to purchase Park Glen for $50,000,000. Pet. App. 44a, 48a. Petitioner drafted the purchase agreement for Park Glen on behalf of Empire. *Id.* at 48a. At the time, petitioner knew that the transaction was being used as a vehicle to get money to IMI, that the fair market value of the Park Glen property at its then-current use (undeveloped land) was only about $4,110,000, and that the approval of the Federal Home Loan Bank Board (FHLBB) was required for the related-party transaction. *Id.* at 44a-49a. Nonetheless, at the next regular meeting of State Savings's board of directors, held on March 23, 1984, at which the board was asked to ratify the transaction, petitioner either did not disclose or deliberately misrepresented material facts to Bryan Wilkinson, State Savings's only outside director, before Wilkinson voted to approve the Park Glen transaction. *Id.* at 51a-54a. In addition, on March 30, 1984, the day that the Park Glen transaction closed, petitioner knew that approval for the transaction from the FHLBB had not been sought or obtained, and that the purchase and sale agreement did not include a required provision, that the price would be refunded if FHLBB approval was not obtained. *Id.* at 50a-51a, 54a.

On April 12, 1985, the FLHBB appointed the Federal Savings and Loan Insurance Corporation (FSLIC) receiver of State Savings, due to the bank's insolvency. FSLIC, as receiver, then assigned all of State Savings's claims against its former directors, officers, controlling persons, employees and share-

holders to FSLIC, in its corporate capacity. Pet. App. 17a. The Federal Deposit Insurance Corporation (FDIC) was subsequently substituted for FSLIC as receiver of State Savings.[1]

2. The FDIC brought suit against petitioner, Oldenburg, and other directors of State Savings, seeking recovery of damages sustained as a result of their fraud and negligence in the operation of the bank. After a bench trial, the district court found that State Savings had deliberately paid an inflated price for the Park Glen property to help Oldenburg generate money for his other companies. The court found that Oldenburg, petitioner, and others had conspired to defraud, and had defrauded, State Savings of $26,500,000, and had embarked on a course of conduct to conceal the true facts about the Park Glen transaction from Wilkinson until the transaction was consummated and the $26,500,000 derived from the transaction was distributed to IMI and Oldenburg. The court also found that State Savings had suffered damages in the amount of $22,000,0000 as a result of the conspiracy and the fraud. Pet. App. 65a.[2] The court therefore concluded that FDIC was entitled to recover $22,000,000 from the conspirators. *Id.* at 66a.

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[1] Pursuant to the Financial Institutions Reform, Recovery and Enhancement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, all assets of FSLIC were transferred to the FSLIC Resolution Fund, which is managed by the FDIC. § 215, 103 Stat. 252 (to be codified at 12 U.S.C. 11A(a)). The FDIC, in its capacity as manager of the FSLIC Resolution Fund, was substituted as the plaintiff in this case.

[2] Although the purchase price for the Park Glen property was $50,000,000, $26,500,000 was actually transferred from State Savings to Oldenburg's other entities. Pet. App. 56a-57a. FSLIC was able to sell the property for $4,500,000. *Id.* at 60a.

In reaching its decision on the fraud claim, the district court held that FSLIC was required to demonstrate fraud by a preponderance of the evidence, rather than by clear and convincing evidence. Pet. App. 9a, 67a. The court also held that petitioner could not raise defenses based on the conduct of the receiver in liquidating the assets of the receivership estate, and it therefore excluded evidence proffered by petitioner that the value of the Park Glen property had deteriorated while it was a receivership asset. *Id.* at 10a.

3. The court of appeals affirmed. Pet. App. 7a-14a. The court first ruled that petitioner had waived his contention that the district court erred by applying the preponderance of the evidence standard to the FDIC's fraud claim. *Id.* at 9a. The court concluded that petitioner had not proposed an alternative standard of proof to the district court, had not contested the district court's reliance on the preponderance standard, and had mentioned the issue below only in a separate and distinct context. *Ibid.*

The court of appeals also agreed with the district court that officers and directors of a failed financial institution may not assert state-law defenses of contributory negligence and mitigation of damages against the FDIC, when the FDIC is suing to recover losses sustained by the bank. Pet. App. 10a-11a. Agreeing with "[t]he two circuit courts which have directly addressed this issue," *id.* at 11a, the court concluded that the FDIC "has no duty first to attempt to mitigate the damages attributed to [the former officers and directors] by seeking other, and perhaps less sure, avenues of relief," and it reasoned that "excepting the FDIC from such affirmative defenses

is consonant with the discretionary function exception" to the Federal Tort Claims Act. *Ibid.* The court also remarked that "nothing could be more paradoxical or contrary to sound policy than to hold that it is the public [that] must bear the risk of errors of judgment made by [FDIC] officials in attempting to save a failing institution—a risk which would never have been created but for defendants' wrongdoing in the first instance." *Id.* at 12a.

ARGUMENT

1. Petitioner contends (Pet. 7-15) that, under *O'Melveny & Myers* v. *FDIC*, 114 S. Ct. 2048 (1994), the district court was required to apply the clear and convincing evidence standard of Utah law to the FDIC's fraud claim in this case. The court of appeals concluded, however, that petitioner had waived that contention by failing to present it to the district court. That conclusion presents no significant issue of law warranting this Court's review.

"It is the general rule, of course, that a federal appellate court does not consider an issue not passed upon below." *Singleton* v. *Wulff*, 428 U.S. 106, 120 (1976). While the courts of appeals do have limited discretion to consider issues not properly preserved for appeal, "as where the proper resolution is beyond any doubt, * * * or where 'injustice might otherwise result,'" *id.* at 121, this Court has not suggested that the courts of appeals must always consider an appellant's contentions about the proper burden of proof, when the arguments could have been, but were not, raised in the district court. Although petitioner contends that other courts of appeals would consider the burden of proof issue for the first time on appeal (see Pet. 12-14), this Court has stated that "[t]he

matter of what questions may be taken up and resolved for the first time on appeal is one left primarily to the discretion of the courts of appeals, to be exercised on the facts of individual cases." *Singleton*, 428 U.S. at 121. There is no "general rule" requiring the courts of appeals to take up particular issues for the first time on appeal. *Ibid.*

The court of appeals did not abuse its discretion in deciding that this was not one of the rare cases in which a miscarriage of justice would result if an issue were not heard for the first time on appeal. Petitioner had ample opportunity to raise the burden of proof issue in the district court but failed to do so. Nor does petitioner contend that he was surprised by unforeseen developments in the law. Further review of his arguments about the burden of proof is therefore unwarranted.

2. Petitioner also contends (Pet. 15-19) that the court of appeals erred in concluding that he was not entitled to raise state-law defenses arising out of the FDIC's failure to mitigate the damages resulting from petitioner's wrongful acts and its contributory negligence in its handling of the Park Glen property. He argues that the decision below conflicts with *O'Melveny & Myers* and also with the decision of the Fifth Circuit in *FDIC* v. *Massingill*, 30 F.3d 601 (1994). Those contentions are incorrect.

In *O'Melveny & Myers*, the Court held that state law, rather than federal common law, provides the rule of decision governing the imputation of facts known to insiders of a failed bank to the FDIC when the FDIC sues as receiver of the bank. The Court held that state law supplied the rule of decision applicable to "FDIC's rights and liabilities, as re-

ceiver, with respect to the primary conduct on the part of private actors that has already occurred," but it also observed that the controversy did not involve "the primary conduct of the United States or any of its agents or contractors." 114 S. Ct. at 2055. *O'Melveny & Myers* does not control this case, in which petitioner contends that the FDIC's own actions, after it took control of the bank, should be governed by state law.

The court of appeals agreed with two other circuits that the federal law governing the FDIC's post-receivership conduct in disposing of property owned by the failed bank precludes the assertion of defenses of mitigation of damages and contributory negligence based on that conduct. See *FDIC* v. *Mijalis*, 15 F.3d 1314 (5th Cir. 1994); *FDIC* v. *Bierman*, 2 F.3d 1424 (7th Cir. 1993). As the Seventh Circuit reasoned in *Bierman*:

> It is the duty of the FDIC to manage [a failed bank's] assets in order to replenish the insurance fund that has been used to cover the losses allegedly caused by the directors and officers. When the FDIC undertakes this task, it must act in the public interest. * * * Congress has made it clear that the FDIC is to exercise its discretion in choosing a course of action in its efforts to replenish the fund. * * * [The FDIC] has no duty first to attempt to mitigate the damages attributed to [directors and officers] by seeking other, and perhaps less sure, avenues of relief.

2 F.3d at 1439-1440.

Petitioner relies on *Massingill*, *supra*, but that case concerned the defense of impairment of collateral, not the defense of mitigation of damages. In

Massingill, the Fifth Circuit held that the defendant in that case, who was a co-maker of promissory notes held by a failed bank, could raise a state-law defense of impairment of collateral against the FDIC. The court did not even mention, let alone overturn, its prior decision in *Mijalis*, in which it addressed the different issue presented in this case and adopted the Seventh Circuit's reasoning in *Bierman*. Moreover, since *Massingill* was decided, at least two district courts in the Fifth Circuit have followed *Mijalis* and have held that federal law precludes a defense of mitigation of damages in suits like this one. *RTC* v. *Sands*, 863 F. Supp. 365, 372 (N.D. Tex. 1994) ("[T]he panel [in *Massingill*] ultimately rested its conclusion upon the facts before it * * * and did not purport to hold generally that *O'Melveny & Myers* had superseded the rationale of *Mijalis*."), aff'd mem., 59 F.3d 1241 (5th Cir. 1995) (Table); *FDIC* v. *Schreinder*, No. SA-93-674 (W.D. Tex. Feb. 16, 1995); see also *RTC* v. *Bright*, 157 F.R.D. 397, 401 (N.D. Tex. 1994). There is therefore no conflict between the decision below and decisions of the Fifth Circuit.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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